



Umzinvubu Local Municipality

Audit Report

For the year ended 30 June 2018

Report of the auditor-general to the Eastern Cape Provincial Legislature and the council on Umzimvubu Local Municipality

Report on the audit of the financial statements

Qualified opinion

1. I have audited the financial statements of the Umzimvubu Local Municipality set out on pages ... to ..., which comprise the appropriation statement, the statement of financial position as at 30 June, the statement of financial performance profit or loss and other comprehensive income, statement of changes in net assets and cash flow statement, statement of cash flows and the statement of comparison of budget information with actual information for the year then ended, as well as the notes to the financial statements, including a summary of significant accounting policies.
2. In my opinion, except for the effect of the matters described in the basis for qualified opinion section of my report, the financial statements present fairly, in all material respects, the financial position of the Umzimvubu Local Municipality as at 30 June and its financial performance and cash flows for the year then ended in accordance with the applicable financial reporting framework and the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and Division of Revenue Act of South Africa (Act no. 3 of 2017) (DoRA).

Basis for qualified opinion

Property, plant and equipment

3. The municipality did not adequately address the issues identified in the prior year. Furthermore the municipality did not have an adequate asset management system to record and account for property plant and equipment. I was unable, to obtain sufficient appropriate evidence by alternative means to confirm the carrying value of property, plant and equipment of R799 million (2017: R922,8 million), as disclosed in note 9 to the financial statements. Consequently, I was unable to determine whether any adjustment was necessary to the property plant and equipment.
4. The balance of property, plant and equipment includes depreciation. In these circumstances, I was unable to determine whether any adjustments were required to the depreciation and amortisation as disclosed in statement of financial performance and note 32 at R97,4 million.

Investment property

5. The municipality incorrectly classified infrastructure assets used for basic service delivery as investment property instead of property plant and equipment in accordance with GRAP 17, *Property plant and equipment*. Consequently, investment property is overstated by R30,2 million and (2017: R30,2 million) and infrastructure assets are understated by R30,2 million (2017: R30,2 million).

Expenditure

6. Expenditure is overstated by R11,9 million due to transactions that are incorrectly recorded in the 2017/18 financial year, however the services were received in the 2016/17 financial year. Consequently, the comparative figure for payables from exchange transactions disclosed in the statement of financial position is overstated by R 13,6 million.

Context for the opinion

7. I conducted my audit in accordance with the International Standards on Auditing (ISAs). My responsibilities under those standards are further described in the auditor-general's responsibilities for the audit of the financial statements section of this auditor's report.
8. I am independent of the municipality in accordance with the International Ethics Standards Board for Accountants' *Code of ethics for professional accountants* (IESBA code) and the ethical requirements that are relevant to my audit in South Africa. I have fulfilled my other ethical responsibilities in accordance with these requirements and the IESBA code.
9. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my qualified opinion.

Emphasis of matters

10. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Irregular expenditure

11. As disclosed in note 49 to the financial statements, irregular expenditure of R139, 4 million was incurred in the year under review as a result of non-compliance with supply chain management (SCM) legislation.

Unauthorised expenditure

12. As disclosed in note 47 to the financial statements, unauthorised expenditure of R 96, 4 million was incurred in the year under review as a result of non-cash items relating to revaluation of assets which yielded larger depreciation than budgeted, as well as transfer of electrical assets to Eskom and impairment of debtors.

Restatement of corresponding figures

13. As disclosed in note 53 to the financial statements, the corresponding figures for 30 June 2017 have been restated as a result of errors in the financial statements of the municipality for the year ended 30 June 2018.

Other matters

14. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unaudited disclosure notes

15. In terms of section 125(2)(e) of the MFMA, the municipality is required to disclose particulars of non-compliance with the MFMA in the financial statements. This disclosure requirement did not form part of the audit of the financial statements and, accordingly, I do not express an opinion thereon.

Unaudited supplementary schedules

16. The supplementary information set out on pages xxx to xxx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.

Responsibilities of accounting officer for the financial statements

17. The accounting officer is responsible for the preparation and fair presentation of the financial statements in accordance with SA Standards of GRAP and the requirements of the MFMA and DoRA, and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.
18. In preparing the financial statements, the accounting officer is responsible for assessing the Umzimvubu Local Municipality's ability to continue as a going concern, disclosing, as applicable, matters relating to going concern and using the going concern basis of accounting unless the accounting officer either intends to liquidate the municipality or to cease operations, or has no realistic alternative but to do so.

Auditor-general's responsibilities for the audit of the financial statements

19. My objectives are to obtain reasonable assurance about whether financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes my opinion. Reasonable assurance is a high level of assurance but is not a guarantee that an audit conducted in accordance with the ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.
20. A further description of my responsibilities for the audit of the financial statements is included in the annexure to this auditor's report.

Report on the audit of the annual performance report

Introduction and scope

21. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report material findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report. I performed procedures to identify findings but not to gather evidence to express assurance.

22. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
23. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2018. My procedures address the reported performance information, which must be based on the approved performance planning documents of the municipality. I have not evaluated the completeness and appropriateness of the performance indicators included in the planning documents. My procedures also did not extend to any disclosures or assertions relating to planned performance strategies and information in respect of future periods that may be included as part of the reported performance information. Accordingly, my findings do not extend to these matters.
24. I evaluated the usefulness and reliability of the reported performance information in accordance with the criteria developed from the performance management and reporting framework, as defined in the general notice, for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2018:

Development priorities	Pages in the annual performance report
KPA2-Basic service delivery	x – x
KPA3-Local economic development	x – x

25. I performed procedures to determine whether the reported performance information was properly presented and whether performance was consistent with the approved performance planning documents. I performed further procedures to determine whether the indicators and related targets were measurable and relevant, and assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
26. I did not raise any material findings on the usefulness and reliability of the reported performance information for the Basic Service Delivery development priorities. The material finding in respect of the usefulness of the Local Economic Development is as follows:

Performance indicator and target not relevant

Indicator: Amount of revenue collected

27. There was no clear link between the indicator, the amount of revenue collected and the target of R 334 400 as well as the key performance area to which it relates. The indicator and related

target focused on collection of revenue in order for the municipality to be financial viable, while the key performance area aimed to achieve local economic development.

Other matters

28. I draw attention to the matters below.

Achievement of planned targets

29. Refer to the annual performance report on pages x to x; x to x for information on the achievement of planned targets for the year. This information should be considered in the context of the qualified opinion expressed on the usefulness and reliability of the reported performance information in paragraph(s) x; x; x of this report.

Adjustment of material misstatements

30. I identified material misstatements in the annual performance report submitted for auditing. These material misstatements were on the reported performance information of KPA 2: Basic services delivery and KPA 3: Local economic development.

31. As management subsequently corrected the misstatements on KPA 2 Basic services delivery, I did not raise material findings on the reliability of the reported performance information.

Report on the audit of compliance with legislation

Introduction and scope

32. In accordance with the PAA and the general notice issued in terms thereof, I have a responsibility to report material findings on the compliance of the municipality with specific matters in key legislation. I performed procedures to identify findings but not to gather evidence to express assurance.

33. The material findings on compliance with specific matters in key legislations are as follows:

Annual financial statements and annual report

34. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122(1) of the MFMA. Material misstatements identified by the auditors in the submitted financial statements were not adequately corrected and the supporting records could not be provided subsequently, which resulted in the financial statements receiving a qualified audit opinion.

Expenditure management

35. An adequate management, accounting and information system was not in place which recognised expenditure when it was incurred, as required by section 65(2)(b) of the MFMA.

36. Reasonable steps were not taken to prevent irregular expenditure, as required by section 62(1)(d) of the MFMA. Most of the disclosed irregular expenditure was caused by non-compliance with SCM regulations 32 and 36. Irregular expenditure amounting to R16, 9 million was incurred on Tyinirha Bridge, Construction of landfill site KwaBhaca, Maintenance of Huku

Community Hall, Maintenance of Dandala Street, Lubhalasi Access Road, Supply and Delivery of Agricultural Inputs and Asset Register Overhaul.

Asset management

37. An effective system of internal control for assets, including an asset register, was not in place, as required by section 63(2)(c) of the MFMA.

Other information

38. The accounting officer is responsible for the other information. The other information comprises the information included in the annual report. The other information does not include the financial statements, the auditor's report and those selected development priorities presented in the annual performance report that have been specifically reported in this auditor's report.
39. My opinion on the financial statements and findings on the reported performance information and compliance with legislation do not cover the other information and I do not express an audit opinion or any form of assurance conclusion thereon.
40. In connection with my audit, my responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements and the selected development priorities presented in the annual performance report, or my knowledge obtained in the audit, or otherwise appears to be materially misstated.
41. I did not receive the other information prior to the date of this auditor's report. After I receive and read this information and if I conclude that there is a material misstatement, I am required to communicate the matter to those charged with governance and request that the other information be corrected. If the other information is not corrected, I may have to retract this auditor's report and reissue an amended report as appropriate. However, if it is corrected this will not be necessary.

Internal control deficiencies

42. I considered internal control relevant to my audit of the financial statements, reported performance information and compliance with applicable legislation; however, my objective was not to express any form of assurance thereon. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for the qualified of opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report
43. Leadership did not implement controls over the asset management and financial reporting processes such as regular processing and reconciling of transactions. The audit action plan was not implemented and monitored adequately to ensure that the root cause of prior year findings on asset management and compliance with legislation was addressed.
44. The accounting officer did not adequately review and monitor compliance with applicable legislation, with the result that the municipality incurred irregular expenditure due to non-compliance with SCM regulations 29, 32 and 36.

Other reports

45. I draw attention to the following engagements conducted by various parties that had, or could have, an impact on the matters reported in the municipality's financial statements, reported performance information, compliance with applicable legislation and other related matters. These reports did not form part of my opinion on the financial statements or my findings on the reported performance information or compliance with legislation.
46. At the time of this report, an external service provider was conducting an investigation into procurement processes and possible fraud committed on the electronic national administration traffic information system (eNATIS). The investigation was in progress and the expected date of the outcome is unknown.

Auditor – GENERAL

East London

30 November 2018



AUDITOR - GENERAL
SOUTH AFRICA

Auditing to build public confidence

Annexure – Auditor-general's responsibility for the audit¹

1. As part of an audit in accordance with the ISAs, I exercise professional judgement and maintain professional scepticism throughout my audit of the financial statements, and the procedures performed on reported performance information for selected development priorities and on the municipality's compliance with respect to the selected subject matters.

Financial statements

2. In addition to my responsibility for the audit of the financial statements as described in this auditor's report, I also:
 - identify and assess the risks of material misstatement of the financial statements whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for my opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or the override of internal control.
 - obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the municipality's internal control.
 - evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the board of directors, which constitutes the accounting officer
 - conclude on the appropriateness of the accounting officer's use of the going concern basis of accounting in the preparation of the financial statements. I also conclude, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the municipality's ability to continue as a going concern. If I conclude that a material uncertainty exists, I am required to draw attention in my auditor's report to the related disclosures in the financial statements about the material uncertainty or, if such disclosures are inadequate, to modify the opinion on the financial statements. My conclusions are based on the information available to me at the date of this auditor's report. However, future events or conditions may cause a municipality to cease operating as a going concern.
 - evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
 - obtain sufficient appropriate audit evidence regarding the financial information of the municipality to express an opinion on the financial statements. I am responsible for the direction, supervision and performance of the audit. I remain solely responsible for my audit opinion.

Communication with those charged with governance

3. I communicate with the accounting officer regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that I identify during my audit.
4. I also confirm to the accounting officer that I have complied with relevant ethical requirements regarding independence, and communicate all relationships and other matters that may reasonably be thought to have a bearing on my independence and, where applicable, related safeguards.

--